

Memorandum



Subject Interview With [REDACTED]

Date May 15, 1996

60-2096-0002

To Frito File

From Neeli Ben-David *JD*

Nina Hale interviewed [REDACTED]

70

BACKGROUND

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

¹ [REDACTED]

distribution: RWF, DNK, HALE, PTACEK, ALEXANDER - EAG, SWEENEY, JONES,
BEN-DAVID, CASE, CHRON, ARCHIVE

REVENUE

b4,7D

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

The "snack war" (also "chip war") grew out of the advent of Eagle into the salty snack foods market. Previously, the market was dominated by local and regional companies with one national company, Frito Lay. [REDACTED]

[REDACTED]

[REDACTED]

Anheuser Busch decided to enter all markets at the same time and begin distributing nationally under the brand name Eagle. This endangered all of the regional salty snack food companies. [REDACTED]

[REDACTED]

7D

[REDACTED]

[REDACTED]

[REDACTED]

"THE CHIP WAR"

The chip war consisted of a fight between the two big brands on the national market. Eagle devoted its resources to competing nationally with Frito. As a result of this competition between the two big brands, a lot of the regionals could not retain their market shares. [REDACTED]

Before the chip war, Frito would take a price increase once a year and the regionals would follow suit. Once Eagle came in, Eagle would act and Frito would respond more frequently than once a year. This activity caught all the regionals in the crossfire. Suddenly shelf space, promotional advertising and spending increased. Frito worked to get all the regionals out of business to cut down on its own competition.

Frito began offering money for shelf space and cooperative advertising to the retailers. It began cutting wholesale prices and increasing consumer advertising. In order to keep up, regionals had to cut consumer spending. Eventually, "customer"

referred to the retailer rather than the consumer. Vendors began to come under the control of the retailer. They had to buy the opportunity to show their wares to the retailer. They no longer had control over the vendor-retailer relationship. In many instances, profit was given up altogether.

Vendors began bargaining over the price of shelf space. In addition, they had to cut back significantly on investment spending in the company which reduced product quality and innovations. Increasingly, vendors focused on short term goals; that is, how to keep what shelf space they had and how to keep sales steady in order to justify the space.

Eagle ended up getting approximately 15 percent of the market share prior to going out of business. Frito raised its market share during the chip war from 45 - 50 percent to 55 - 60 percent.

GEOGRAPHIC MARKET

[REDACTED]

[REDACTED]

[REDACTED]

7D

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Exempt under b7D

b4, 7D

[REDACTED]

[REDACTED]

[REDACTED]

BELL MARKING

Convenience store retailers were upset with Frito's habit of "bell marking." Bell marking consists of pre-pricing a bag and then selling it to the retailer at a fixed price. For example, the price on the bag would read \$.99 and Frito would sell at \$.74.

This limits the retailer to a 25 percent profit margin and does not allow the retailer any leeway with regard to how much of a profit margin it can demand. Usually retailers at convenience stores get a 30 to 40 percent profit margin, so Frito's pre-pricing is well below what they have come to expect. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

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Exempt under b4, b7D

EXCLUSIVITY

[REDACTED] claims that there is not much exclusivity within convenience stores. However, there are significant barriers to entry for regional companies. For example, [REDACTED]

[REDACTED] Frito does, it is easier for Frito to make demands on 7-Eleven. Frito can create a national program and present it to its corporate headquarters and get 7-Eleven to give it advantages in such areas as display and shelf space. 7D

DATA SERVICES

[REDACTED]

Frito provides marketing information on which many retailers base their decisions. They often manipulate the data and present it in a way most favorable to Frito.

Frito employees often serve as aisle captains for the various chains. This means that a Frito employee will have his own office with the retailer, spending 40 hours a week manipulating the data that the retailer can use to determine the allocation of shelf space. While [REDACTED] finds this practice unfair, it also notes that this is just competition and [REDACTED] must deal with it. It is just one of the rules of the game.

SLOTING FEES

However, [REDACTED] feels that slotting fees constitute a gross unfairness. [REDACTED] is that the major nationals have a huge advantage over regionals in the cost of extra space, since the cost ends up being a larger percentage of the regionals' then of the nationals' spending. National companies will pay any price just to get shelf space, whereas regionals are unable to do this. 7D

[REDACTED] does not have the money to do what Frito is doing. Frito can produce at approximately a [REDACTED] cheaper cost because of its greater volume and economies of scale. For example, it can issue a huge trade ad and reap the benefits nationally, whereas a regional company can not do this. The amount that Frito has paid for space costs them less of an increase as a percentage of overall spending because of Frito's large volume space. One particular example: [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] 7D

[REDACTED] noted that Frito now is in a habit of being in a snack war and is continuing to act as if Eagle is still in the market.

SHELF SPACE

How much a particular company is selling determines how much space it can buy. Even if a company cuts its wholesale price to the retailers to allow the retailers a larger profit margin, retailers will not use this to determine space allocation. They base their space allocation entirely on volume sales.

[REDACTED] noted that a typical retailer has two different profit centers which are completely separate. The first one is real estate, the selling of their shelf space; and the second is revenues from his products. Even though a retailer would be making more profit off of a particular vendor, it does not necessarily follow that he would be willing to allocate more shelf space to that vendor. Frito allows retailers [REDACTED] b4, 7D

[REDACTED] Even so, retailers are still willing to sell more shelf space to Frito, if it offers a high enough price.

PREDICTIONS

Since Eagle has disappeared from the market, the number of Frito discounts has declined significantly. In addition, there is a rumor that Frito's list price (i.e., the price it sells its product to retailers) will be going up. [REDACTED] predicts that Frito will not want to increase its market share, which is now around [REDACTED] nationally, in order to stay out of any kind of antitrust trouble. Instead, it will focus on gathering more market share in areas where Nielsen does not track (e.g., mom and pop stores). Also Frito will focus on increasing its profitability.

[REDACTED]

[REDACTED]

[REDACTED]

So/So # 10810